10. UNITED KINGDOM

10.1. General

What comes closest to the Austrian private foundation in the United Kingdom is the *trust*. This survey describes the most frequent forms of the *private family trust* as the legal form that is the most similar to the private foundation we know.

The persons involved are the *trustee*, the *beneficiary*, and the *settlor*. The settlor is the person who endows money, investments, land or buildings or other assets, such as paintings, to the trust. This may happen when the trust is formed or at a later point in time.

A trust is established by means of a *trust deed*. This may also be based on a final will. The *trustee* manages the assets endowed while the beneficiaries benefit in one form or another from these assets.

In the UK, there are different forms of trusts, such as:

- bare trusts
- interest in possession trusts
- discretionary trusts
- accumulation and maintenance trusts
- mixed trusts
- settlor-interested trusts
- non-resident trusts
- special trusts

10.2. Bare Trust

This trust form is also referred to as *simple trust*. In this form of trust, the beneficiary has immediate and full right of disposition to the assets and the income earned. The rights of the trustee under the name of which the assets are held are very limited. The trustee has no active obligations either.

Taxation
The beneficiary is personally taxed, that is, he or she is taxed as if the *bare trust* did not exist. The beneficiaries must declare income earned in their personal income tax declaration.

Also in the event that the trustee takes care of the payment of the taxes on behalf of the beneficiary, it is the beneficiary who is tax-liable.

10.3. Interest in Possession Trust

In this form of trust, the beneficiary, in this case also called the *income beneficiary*, is entitled to receive the income generated by the trust. The trustee must give the entire income of the trust (after deduction of expenses incurred and taxes paid by him) to the income beneficiary. It is possible that the beneficiary is entitled to receive these payments for his entire life, in which case he is referred to as a *life tenant*.

The income beneficiary has however no claim to the trust's capital. In most cases, the capital is destined for another beneficiary and intended for payments at a future date (which is usually determined in advance). Such a beneficiary is called a *remainderman* or a *capital beneficiary*. *Interest in possession trust*, the trustee has more rights than in the bare trust. For instance, he may also make payments to the beneficiary out of the trust capital.

Taxation

The trustee is tax-liable for all income earned, in particular:

- Rental and trading income is subject to a base rate of currently 22%.
- Dividend income realised in the UK is subject to the regular dividend tax rate of currently 10%; the tax credit associated with the net dividend reduces the taxes to be paid be the trustee.
- Income from savings (such as interest) is subject to a reduced rate of currently 20%. Income which is already subject to final taxation at source is accordingly deducted from the tax assessment basis.

The beneficiaries receive the payments after deduction of the taxes and fees that the trustee has paid out of the income. The income is used for certain purposes and the trustee's expenses need to be covered, too.

Payments to the beneficiaries are subject to the regular tax rates; however the beneficiaries receive a tax credit for taxes paid by the trustee.

In the event that a beneficiary is in the lowest bracket or tax-exempt at all, he may have a part or all of the taxes paid refunded. There are however no tax credits for dividend taxes. If a beneficiary is in a higher tax bracket, he or she must make additional tax payments.

Only very few *interest in possession trusts* are taxed at special rates. However, in some cases special rates may apply, for instance when a company buys back own shares from the trustees or where the trust involves *vulnerable beneficiaries* (these are beneficiaries that need special protection).

10.4. Discretionary Trust

The trustee has more discretionary power as to the use of income generated by the trust assets. Even if he has received instructions on who the beneficiaries should be, he can decide on the amount to be paid, which beneficiaries or groups of beneficiaries are to receive the payment, how often, and on the terms of the payments.

It is in his discretion to distribute or retain income realised. If the trust income is not distributed to the beneficiaries, it becomes part of the trust assets.

Taxation

The trustees are subject to taxation at special rates for the income earned. Dividends and similar other income are to be taxed at the dividend trust rate (32.5% since 2004-2005), and further income is to be taxed at the rate applicable to trusts (40% since 2004-2005). Since 2005-2006, the first GBP 500 of the trust income are, depending on the nature of the income, either subject to a basic rate of currently 22%, a reduced rate of 20%, or the normal dividend rate of 10%. (Before 2005-2006, this amount was subject to a special rate.)

The income received by the beneficiaries has already been subject to a 40% deduction which is the rate currently valid for trusts. The payments are thus treated as if they were made after deduction of tax. If, however, the beneficiaries are base-rate taxpayers or are not tax-liable at all, they may have the tax refunded. If they are subject to a higher tax rate than the 40% applied, no further tax will be due.

If the trustee is authorised to retain income, he can transform the income into capital. If this capital is then paid out in later years, it is no longer considered a distribution of income, but capital paid out, which is not subject to taxation.

Since 2004/2005, particular regulations apply to beneficiaries deserving special protection; these are persons who are mentally or physically disabled or persons who are under the age of 18.

10.5. Accumulation and Maintenance Trust

The beneficiaries have a claim to the assets (or at least to the income from the assets) only after they have reached a certain age (age of 25 at the latest). In the meantime, the trustees may either use the income to maintain the beneficiary or retain the income generated in the trust.

Taxation

During the period in which the income is retained in the trust (accumulation period), both the trustee and the beneficiaries are subject to taxation (as in the case of a *discretionary trust*).

If the oldest beneficiary is over a certain age – usually 25 – and the accumulation period is not over yet, the trust is treated like a *mixed trust* for tax purposes.

When the accumulation phase has ended, the applicable tax rules depend on what is going to happen with the trust. If the trust is to be dissolved and the trust assets are to be transferred to the beneficiaries, the trustees may have to pay *capital gains tax* on the profits earned as of that date.

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10.6. Tax Pool

The managers or trustees of *discretionary trusts* or *accumulation and maintenance trusts* must make sure that the taxes have been paid before they distribute income to the beneficiaries.

The tax pool is composed of taxes that have been paid by the trustee at the rate required (trust or dividend-trust rate) and of taxes paid at the standard rate applicable to the first GBP 500 of income. The tax credits, such as for dividends, are not included in the tax pool. When the trustees distribute income to the beneficiaries, the tax pool is reduced by the amount of the tax credit on this portion of income.

If the taxes in the pool do not completely cover the tax credit for the beneficiaries, the trustee must come up with the remainder himself.

10.7. Mixed Trust

Most trust forms may also be combined, such as, for example, an *interest in possession trust* with a *discretionary trust* or an *accumulation and maintenance trust*. These trusts are then called *mixed trusts*.

Trustees as well as beneficiaries in a *mixed trust* always pay the tax rates stipulated for the respective portion of income.

Some other forms of mixed trusts exist: In the *settlor-interested* trust, the *settlor* keeps some particular rights, for instance as to the income generated. In *non-resident trusts*, all or some of the trustees do not live in the UK. The *special trusts* are founded for charitable purposes as well as for pension funds, investment funds or employee provision funds.

10.8. Trusts and Capital Gains

Trustees are subject to taxation for all profits that exceed a specific tax-exempt amount; the applicable tax rate depends on the form of the trust. The beneficiaries do not make any payments to the tax authorities with respect to the trust profits, but cannot claim any tax refund on payments made by the trustees either.

Annual tax exemption for trusts is half the amount of the exemption granted to an individual. Only under certain conditions, for example when a trust serves to benefit a disabled person, the trustee is subject to the same tax exemption as an individual.

If a settlor has several trusts, the annual tax exemption is correspondingly limited, proportionally based on the number of settlements formed since 6 June 1978 and which are still in existence.